

Message Text

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ACTION EB-08

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R 110014Z APR 78
FM AMEMBASSY OTTAWA
TO SECSTATE WASHDC 6981
INFO AMCONSUL MONTREAL
USMISSION GENEVA
AMCONSUL HALIFAX POUCH
AMCONSUL CALGARY POUCH
AMCONSUL QUEBEC POUCH
AMCONSUL TORONTO POUCH
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TAGS: EMIN, CA
SUBJECT: FEDERAL-PROVINCIAL FOLLOW-UP ON FIRST MINISTERS
CONFERENCE: NEW HOPE FOR CANADA'S MINING INDUSTRY?

REF: (A) OTTAWA 927 NOTAL; (B) OTTAWA 1707 NOTAL

1. SUMMARY: CANADIAN MINING INDUSTRY OFFICIALS ARE
GREATLY ENCOURAGED BY WHAT THEY VIEW AS IMPROVED PROSPECTS
FOR FEDERAL-PROVINCIAL COOPERATION ON MINERAL TAXATION
THAT WILL HELP TO REVERSE RECENT DECLINE OF INVESTMENT IN
THE INDUSTRY. COMMITMENTS MADE DURING FIRST MINISTERS
ECONOMIC SUMMIT AND MARCH 17 MEETING OF FEDERAL CABINET
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WITH LEADING INDUSTRY OFFICIALS INDICATED TO MINING FIRMS
THAT BOTH LEVELS OF GOVERNMENT REALIZE EXISTING POLICIES
ARE HURTING INDUSTRY AND THAT GOVERNMENTS WILL GIVE SERI-
OUS CONSIDERATION TO INDUSTRY PROPOSALS TO EASE TAX BURDEN
AND RATIONALIZE OVERALL MINERAL PRODUCTION TAX STRUCTURE
ON NATIONAL BASIS. NEWS COVERAGE AND CONVERSATIONS WITH
INDUSTRY OFFICIALS INDICATE GENERAL OPTIMISM, EVEN MILD

EUPHORIA, IN INDUSTRY AS RESULT OF THESE DEVELOPMENTS. INDUSTRY VIEWS THEM AS TURNING POINT ON ROAD TO RESOLVING ITS HISTORIC PROBLEM OF TAX LAYERING. OTHER SOURCES, HOWEVER, PARTICULARLY IN FEDERAL DEPARTMENT OF FINANCE, ARE NOT AS OPTIMISTIC. THEY BELIEVE, AND EMBASSY CONCURS IN THIS VIEW, THAT WHILE CLIMATE FOR FEDERAL-PROVINCIAL COOPERATION IS IMPROVED, GENERAL TENSION IN FEDERAL-PROVINCIAL RELATIONSHIP IS SUCH THAT QUICK TRUCE ON THIS ISSUE--PARTICULARLY BECAUSE IT ENGAGES VERY SENSITIVE POLICY AREA OF RESOURCE MANAGEMENT--IS UNLIKELY. END SUMMARY.

2. CANADIAN BUSINESS PRESS OVER RECENT WEEKS HAS GIVEN PROMINENT COVERAGE TO GROWING OPTIMISM IN MINING INDUSTRY THAT ITS SERIOUS TAX PROBLEM MAY BE RECEDING. PROBLEM, ACCENTUATED BY INDUSTRY'S LONGER-THAN-NORMAL DOWNCYCLE OF REDUCED DEMAND AND WEAK SELLING PRICES, IS THAT OVER LAST SIX YEARS THERE HAS BEEN SUCCESSION OF COMPLEX AND UNCOORDINATED TAX CHANGES BY FEDERAL AND PROVINCIAL GOVERNMENTS. PROVINCES STARTED FEUD WITH NEW MINERAL IMPOSTS. OTTAWA RESPONDED TO WHAT IT CONSIDERED INTRUSION INTO FEDERAL DOMAIN BY REFUSING TO RECOGNIZE PROVINCIAL TAXES AS ALLOWABLE DEDUCTION. THERE WAS SOME ATTEMPT TO AMELIORATE CONFLICT WITHOUT EITHER SIDE BEING PERCEIVED AS GIVING ANY GROUND. THROUGHOUT, INDUSTRY HAS BEEN CAUGHT IN CROSSFIRE. UNCERTAINTIES OVER GOVERNMENT POLICIES HAS LIMITED OFFICIAL USE

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CAUSED DECLINING CONTRIBUTION BY MINING INDUSTRY TO EMPLOYMENT AND EXPORTS. ARTICLES IN "GLOBE AND MAIL," "FINANCIAL POST," AND "NORTHERN MINER" QUOTE MINING ASSOCIATION OF CANADA (MAC) OFFICIALS WHO SEE EMERGING TREND TOWARD FEDERAL-PROVINCIAL COOPERATION AIMED AT HELPING MINING INDUSTRY OUT OF THIS PREDICAMENT BY RATIONALIZING FEDERAL-PROVINCIAL TAX STRUCTURE.

3. MAC OFFICIALS' OPTIMISM STEMS FROM MARCH 17 MEETING WITH FEDERAL CABINET MINISTERS--CALLED AS FOLLOW-UP TO FEDERAL-PROVINCIAL UNDERTAKINGS AT FIRST MINISTERS ECONOMIC SUMMIT--TO DISCUSS MAJOR PROBLEMS FACING MINING INDUSTRY. DURING MEETING, MAC PRESENTED BRIEF TO CABINET WHICH PROPOSES THAT: (1) PRESENT GRADUATED PROVINCIAL MINING TAX RATES BE REPLACED BY FLAT RATE SO COMBINED FEDERAL-PROVINCIAL TAX DOES NOT EXCEED 50 PERCENT, 2) FEDERAL INCOME TAX BE MODIFIED TO ENCOURAGE PROVINCES TO REFORM THEIR TAXES AND (3) AT LATER STAGE DIFFERENT TAX SYSTEMS IN DIFFERENT PROVINCES BE REPLACED WITH ONE COMMON NATIONAL BASE INCLUDING FURTHER LOWERING OF COMBINED FEDERAL/PROVINCIAL RATE TO MAXIMUM OF 40 PERCENT. MAC ALSO PROPOSES THAT SPECIAL INCENTIVES BE PROVIDED TO EN-

COURAGE EXPLORATION AND NEW MINERAL DEVELOPMENT AS WELL
AS OTHER MEASURES TO AID MINING INDUSTRY.

4. NOTING THAT CANADIAN MINING INDUSTRY IS THREATENED BY
DEPRESSED INTERNATIONAL MARKET PRICES THAT ARE IN PART
RESULT OF POLICIES OF SOME LDC GOVERNMENTS, ENERGY MINES

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AND RESOURCES (EMR) MINISTER ALASTAIR GILLESPIE TOLD
PRESS AFTER MEETING THAT HE WOULD BE WILLING TO EXPLORE
WITH INDUSTRY REPRESENTATIVES POSSIBILITY OF INTERNATIONAL
MINERAL "ARRANGEMENTS" TO PROTECT MINING INDUSTRY. MAC
REPRESENTATIVE ALFRED POWIS, CHAIRMAN OF NORANDA MINES
LTD., COMMENTED THAT INDUSTRY DOES NOT FAVOR INTERNATIONAL
MARKET RIGGING. HE OBSERVED THAT MARKETS MAY NOT WORK
PERFECTLY BUT ARE PREFERABLE TO CARTELS. CANADIAN MINING
FIRMS WOULD PREFER COMPETITIVE INTERNATIONAL MARKETS EVEN
IF COMPETITION INCLUDES GOVERNMENT-SUPPORTED MINES IN
OTHER COUNTRIES. POWIS WHO WAS REPORTEDLY ENCOURAGED BY
TENOR OF MEETING, STRESSED THAT "INDUSTRY NEEDS ASSURANCE
IT WILL NOT BE CUT OFF AT THE KNEES BY TAXATION WHEN IT
RECOVERS FROM POOR CURRENT MARKET CONDITIONS." EDITORIAL

COMMENT ON MEETING HELD THAT PRESENT FEDERAL-PROVINCIAL
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TAX STRUCTURE IS GREATER DETERRENT TO FUTURE GROWTH AND
EXPANSION OF CANADA'S MINING INDUSTRY THAN INTERNATIONAL
MARKET CONDITIONS.

5. COMMENT: EMR SOURCES TELL US THAT GILLESPIE'S STATE-
MENT ABOUT POSSIBLE INTERNATIONAL ARRANGEMENTS TO STA-
BILIZE METAL MARKETS IS SO FAR JUST PUBLIC MUSING OVER
PROBLEM WHICH HAS CAUSED FEDERAL GOVERNMENT GOOD DEAL OF
POLITICAL EMBARRASSMENT DURING PAST YEAR. WITH THOUSANDS
OF WORKERS UNEMPLOYED AT MINING CENTERS LIKE SUDBURY AND
CANADIAN SHARE OF WORLD NICKEL PRODUCTION DROPPING FROM
60 TO 35 PERCENT OVER RECENT YEARS, GILLESPIE AND HIS
CABINET COLLEAGUES ARE UNDER PRESSURE TO DO SOMETHING.
SOURCES, HOWEVER, TELL US THAT GILLESPIE HAS NO FIRM IDEAS
NOR ARE THERE ANY SPECIFIC PLANS BREWING IN EMR. CANADA'S
LIKELY APPROACH TO THIS PROBLEM WILL BE TO PRESS FOR ESTAB-
LISTMENT OF PRODUCER-CONSUMER FORA SIMILAR TO LEAD-ZINC
STUDY GROUP FOR OTHER MINERALS. THIS WOULD BE PURSUED IN
UNCTAD OR POSSIBLY OTHER AS YET UNDETERMINED INTERNATIONAL
FORA.

6. INDUSTRY REPRESENTATIVES TELL US THAT THEY GENERALLY
AGREE WITH THIS STRATEGY. INTERMEDIATE MEASURES SUCH AS
STUDY GROUP APPROACH MIGHT BE USEFUL, BUT OTHERWISE THEY
WANT TO CONTINUE BUSINESS AS USUAL. INDUSTRY IS STRONGLY
OPPOSED TO DIRECT GOVERNMENT INTERVENTION--CARTELS OR
NICKEL STOCKPILE SUGGESTED BY PRIME MINISTER TRUDEAU LAST
OCTOBER.

7. IMPLICATIONS FOR DOMESTIC POLICY CHANGE, HOWEVER, WERE
MOST HOPEFUL SIGNS FOR INDUSTRY TO COME OUT OF MARCH
17 MEETING. MAC OFFICIALS TELL US THAT THEIR SESSION WITH
FEDERAL CABINET WAS "TURNING POINT" ON ROAD TO RESOLUTION
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OF REALLY SERIOUS PROBLEMS INDUSTRY HAS EXPERIENCED AS
RESULT OF RECENT FEDERAL-PROVINCIAL DISPUTES OVER MINERALS
TAXATION POLICY. FEDERAL MINISTERS WENT TO SOME LENGTH AT
MEETING TO ASSURE MAC REPS THEY ARE SERIOUSLY CONCERNED
AND INTEND TO DO SOMETHING ABOUT PROBLEM. THEY INDICATED,
THOUGH, THAT PROVINCES ARE OBSTACLE. BUT MAC ALSO SEES
FIRM INDICATIONS THAT PROVINCES WILL TAKE NECESSARY PARAL-
LEL ACTIONS TO REVISE OVERALL MINERAL TAX STRUCTURE. BOTH

LEVELS OF GOVERNMENT, ACCORDING TO MAC, HAVE BEEN SHAKEN BY DRAMATIC FALL-OFF IN MINING INDUSTRY INVESTMENT. THEY REALIZE THAT FEDERAL-PROVINCIAL DISPUTES OVER MINERAL REVENUE SHARING HURT INVESTMENT CLIMATE, THEY SEE NEED TO AVOID SUCH CONFRONTATION IN FUTURE AND INTEND TO MODIFY TAX LAW TO CORRECT SITUATION. KEY TO THIS SHIFT IN GOVERNMENT ATTITUDES IS REALIZATION THAT WHILE INVESTMENT CLIMATE IS SENSITIVE TO SMALL CHANGES IN MINERAL TAX STRUCTURE, EVEN AT HIGHEST POSSIBLE RATES MINERAL TAXES ARE NOT SIGNIFICANT REVENUE EARNERS.

8. MAC IS PARTICULARLY ENCOURAGED BY WHAT IT SEES AS SIGNIFICANT MOMENTUM DEVELOPING TO RATIONALIZE OVERALL MINERAL TAX STRUCTURE. AS RESULT OF ECONOMIC SUMMIT AND MARCH 17 MEETINGG.SERIES OF FEDERAL-PROVINCIAL DEPUTY MINISTERS MEETINGS WILL BE HELD, BEGINNING WITH ONTARIO IN MAY AND FOLLOWED BY BRITISH COLUMBIA, MANITOBA, SASKATCHEWAN AND QUEBEC IN JUNE AND JULY. MINISTERIAL-LEVEL TALKS WILL FOLLOW LATER. FOR FIRST TIME AT SUCH INTER-GOVERNMENTAL TALKS, MAC HAS BEEN ASKED TO PREPARE BASIC INFORMATION PAPERS.

9. OTHER INFORMED OBSERVERS HERE, HOWEVER, DO NOT SHARE MAC'S ENTHUSIASM ABOUT THESE RECENT DEVELOPMENTS. SOURCES IN FINANCE DEPARTMENT TELL US THAT FEDERAL GOVERNMENT IS NOT PREPARED TO MAKE MAJOR CONCESSIONS IN MINERAL TAX POLICY. CONCESSIONS FOR MOST PART WILL HAVE TO COME FROM PROVINCIAL SIDE. MOREOVER, FINANCE OFFICIALS SAY MAC'S TIDY LIMITED OFFICIAL USE

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PROPOSAL FOR REDUCING COMBINED FEDERAL-PROVINCIAL TAX RATE FIRST TO 50 PERCENT, THEN TO 40 PERCENT, IN UNIFORM NATIONAL STURCTURE IS SIMPLY UNREALISTIC AND WILL NEVER GET OFF THE GROUND. WHILE FINANCE CONCEDES THAT ATMOSPHERE HAS CHANGED SINCE MID-1970'S AND BOTH LEVELS OF GOVERNMENT APPRECIATE NEED FOR COOPERATION, PROGRESS WILL BE DIFFICULT AT BEST.

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10. EMBASSY SHARES THIS LATTER VIEW OF POTENTIAL FOR
FEDERAL-PROVINCIAL COOPERATION ON MINERAL TAX POLICY.
THERE IS SIMPLY TOO MUCH FRICTION IN OVERALL FEDERAL-
PROVINCIAL RELATIONSHIP--PARTICULARLY IN SENSITIVE RE-
SOURCE POLICY AREA--TO DECLARE TRUCE ON THIS ONE ISSUE
AND SOLVE MINING INDUSTRY'S TAX PROBLEMS AT A BLOW. AND
EVEN IF SIGNIFICANT PROGRESS ALONG THESE LINES DOES DE-
VELOP, INDUSTRY STILL FACES VERY SERIOUS DIFFICULTY DUE
TO TROUBLED INTERNATIONAL MARKET. ENDERS

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